CONSEQUENCES OF FRAUD AT THE PRESENTATION OF THE FINANCIAL STATEMENTS

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Abstract: The field of tax evasion has generally been the subject of research at different levels on a number of occasions. However, reality demonstrates that tax fraud today is far from being properly and completely perceived, so the mechanisms designed to prevent and combat it are far from being effective.Tax evasion is a very difficult concept to express, and there is no clear definition of tax fraud. When it comes to fraud, there is also talk of legal or legitimate fraud, illegal fraud, international evasion, legal and illegal evasion, tax havens or refugees, abuse of the right to flee to the tax, freedom to choose the least taxed way, or fiscal underestimation, law fraud or underground economy.

JEL classification: M41, M42

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1. INTRODUCTION

In any democratic state, the taxpayer is considered to be a subject of good faith law and, as a result, the tax obligations which he undertakes (enrolling them in the tax return) is the foundation on which the tax administration is based when establishes and enters in the tax receivables the amounts of taxes due. The taxpayer's tax (tax system) report is above all a perceived problem of the entire levy he has to pay. This perception is obviously characterized by a sense of constraint, even by pressure, which explains the permanent opposition to tax (rejection). Despite these realities, the most conscientious among taxpayers necessarily feel the tax levy as an amputation unjust or at least inappropriate personal wealth. Most often, the tax is perceived as a sacrifice.

2. FRAUDATION OF FINANCIAL STATEMENTS AND RESPONSIBILITY OF THE FINANCIAL AUDITOR

The fraud involves a series of irregularities and illegal actions characterized by deliberate circumvention in order to obtain financial advantages. The three key factors that indicate frugal activity: fiscal pressure, the recognized opportunity is a way to reasonably explain the adopted behavior.

The field of tax evasion, respectively fraud, is an extremely controversial area, and the degree of auditor's accountability in the prevention and detection process has generated quite a lot of heated debates in recent years. In planning and performing the audit, in order to reduce risk to an acceptable level, the auditor should consider the risk of material misstatement in the financial statements due to fraud.

ISA 240 "*Auditor's Responsibilities for Fraud in an Audit of Financial Statements"* was issued in December 2006 and entered into force for audits of financial statements starting with December 15, 2008. This standard distinguishes between fraud and error and describes two types of fraud which are relevant to the auditor, **ie misstatements resulting from the misstatement of the assets and the misstatements resulting from fraudulent financial reporting**; describes the responsibilities of those charged with the governance and the entity's leadership for fraud prevention and detection, describes the inherent limits of the audit in the context of fraud, and establishes the auditor's responsibilities for detecting significant misstatements due to fraud.

Generally, fraud can be defined as the activity by which a natural or legal person acts with the intent of obtaining an illegitimate benefit, violating a legal and contractual obligation.

The notion of fraud should be perceived and examined in a distinct manner in relation to the inconsistencies of Article 953 of the Civil Code, according to which "*creditors may, in their own name, attack the actions of the debtors in damaging the rights. In any form of fraud, bad faith is concretized by an illicit act".*[1]

Fraud may fall within the scope of civil law, with the consequences provided by art. 998 of the Civil Code, or under the incidence of the criminal law, in this case arguing both criminal liability and tort liability. In both situations, the existence of material or moral damages is one of the essential elements of fraud. Fraud may concretize in an act, but in many situations it is only the mark of will; in the latter case, fraud is confronted with the bad faith.

Of the many forms and fraudulent activities, I mention the most important ones:

Table no.1 *Forms of fraud*

Forms of fraud	Forms of fraud
1.Fraudulent falsification activity	8. Distribution of unrealized dividends
2.Contraband	9.Fraudulent insolvency organization and continued directed credit, without reasonable assurances of compliance
3.Fraudulent actions and abuses of economic situation by entrepreneurs in multilateral societies	10. Fraudulent practices on illegal work
4.Fraudulently getting subsidies by people who do not have the darn to such funding	11.Money laundering
5.Turning off the use of subsidies for other purposes	12.Illicit practices in real estate sales and purchases of real estate, without ol expert expertise on the fair value of goods
6. Fraudulent practices in information	13. Illegal affairs of bankers, to the profession of professional secrecy, to which the authorities do not have the legal instrument to enter and defuse them
7. Establishment of fictitious capital companies	14.Fiscal fraud

Source:author's concept

[1] Sorin Briciu, C.T (2010)- Consideratii privind responsabilitatea si raspunderea auditorului independent in auditul statutar privind frauda, Revista *Audit* financiar, nr.12/2010

2.1. ASSESSING THE RISKS OF MATERIAL MISSTATEMENT IN ACCORDANCE WITH ISA 240

In planning and performing the audit to reduce risk to an acceptably low level, the auditor should take into account the risk of material misstatement in the financial statements due to fraud. ISA 240 clearly states who has the primary responsibility for preventing and detecting fraud: *"The primary responsibility for preventing and detecting fraud lies with both individuals who are in charge of the governance of the entity and of the management".*[2] ISA 240 goes on to say, however, that: "*An auditor conducting an audit in accordance with ISA is responsible for obtaining reasonable assurance that the financial statements considered in their entirety are free from material misstatement, either as a result of fraud or error "*[3].

We conclude that the entity and the auditor have responsibilities in detecting fraud or error. We could say that management and those charged with governance have the primary responsibility to detect fraud and error, while the auditor has a secondary responsibility.

2.2. FRAUD AND ERROR - CONCEPTUAL DELIMITATION

Distortions of financial statements may occur either as a result of fraud or error. The factor that distinguishes between fraud and errors is the extent to which the action that has led to the distortion of the financial statements is intentional or unintended[4].

In this respect, we say that the non-compliance with the regulatory framework, procedural code violations consisting of omissions, errors or unintended mistakes represent deficiencies, deviations and malfunctions.

The concept of ***"fraud"*** has several meanings, which we present below:

- *fraud is the total of irregularities and illegal actions committed with the intention of deceiving;*
- *fraud means any intelligent action or omission in connection with the use or disclosure of statements or documents.*

On the other hand, the term ***"error"*** refers to unintentional misstatement in the financial statements, including the omission of an amount or a presentation, such as:

- the error in collecting or processing the data on which the financial statements are prepared.
- an improper accounting estimate arising from the overlook or misinterpretation of the facts.
- mistake in applying accounting policies relating to the evaluation, recognition, classification, presentation or disclosure of information;

At the same time, auditors, when planning their business, collecting and evaluating audit evidence, and when expressing their opinion on the financial statements through the audit report, should take into account the risk of material misstatement due to fraud or error.

[2] ISA 240-paragraf 4
[3] ISA 240-paragraf 5
[4] ISA 240 Responsabilitatile auditorului privind frauda in cadrul unui audit al situatiilor financiare

The term *"**fraud**"* refers to a ***deliberate action*** taken by one or more persons within the management, those charged with governance, employees or third parties, ***which involves the use of deceit in order to obtain an unfair or unlawful advantage.*** Although fraud is a vast legal concept, the auditor is concerned about fraudulent ***actions that cause significant misstatement in the financial statements. Distortion of financial statements may not be subject to fraud.***

In this sense, the significance threshold plays an important role. The materiality threshold (materiality level) adopted will be the value against which it is determined whether errors, omissions or mistakes identified in accounts, considered either individually or collectively, indicate whether those accounts provide a true, complete and accurate picture of the outcome, financial position, and property of the enterprise[5].

There is a close correlation to materiality and audit risk. In the "General Framework for the Preparation and Presentation of Financial Statements" of the International Accounting Standards Committee, ***the materiality threshold was defined as follows***: *"Information is meaningful if its omission or erroneous declaration could influence the economic decisions of users taken on the basis of the financial statements.The threshold of significance depends on the size of the element or the error judged in the specific circumstances of the omission or erroneous declaration. Thus, the significance threshold offers rather a limit than a primary qualitative characteristic that information must have in order to be useful.* "

The International Standard of Audit 320 *"Assessment of Significance and Audit Risk by the User"* states that the relationship between the materiality threshold and the audit risk is inversely proportional: the lower the audit risk, the significance level is higher, and vice versa.

In order to determine the level of significance threshold by nature, the auditor should determine whether a non-material item in value can be considered material due to its inherent nature or its characteristics. In this regard, consideration should be given to:

1. *the comparison of audit transactions with the regulations regarding the audited enterprise, as well as with those regulations, which refer to the branch to which it belongs.*
2. *the size of the enterprise, taking into account total assets, total revenues, etc*
3. *business-related factors such as: the date of its establishment, annual profit, turnover, etc*

[5] Glover W.T, S.L(2011)- A guide to Forensic Accounting Investigation. John Wiley&Sons

Source:the author's concept

Figure no.1 Criteria according to which the level of significance threshold is set in the audit engagement for an item

3. JOINT SCHEMES OF FINANCIAL FRAUDS

The Company's management can try to use various accounting techniques to create a financially most advantageous image by defrauding financial reports.

There are two types of deliberate misrepresentation that are relevant - distortions arising from fraudulent financial reporting and misstatements arising from embezzlement of assets.

Fraudulent financial reporting involves intentional distortions or omissions of values or disclosures in financial statements to mislead users. Fraudulent financial reporting can be accomplished through:

- manipulation, falsification or modification of the accounting records or supporting documents on the basis of which the financial statements are prepared;
- misinterpretation or deliberate omission of events, transactions, or other significant information in the financial statements;
- deliberate misapplication of accounting policies related to the evaluation, recognition, classification, disclosure or disclosure of information.

Fraudulent financial reporting often involves avoiding controls by the management that under other circumstances may seem to be working effectively. Fraud can be committed by avoiding controls by management using techniques such as:

- record fictional chapters in the journal, especially close to the end of an accounting period, to manipulate operational results or achieve other objectives;
- inappropriate change of assumptions and change of reasoning used to estimate balance of accounts;
- omission, advancement or delay of recognition in the financial statements of events and transactions that occurred during the reporting period;
- hiding, or non-disclosure, of facts that could affect the amounts registered in the financial statements
- engaging in complex transactions that are structured to misrepresent the entity's financial position or financial performance; and
- changing records and terms for important and unusual transactions.

Fraudulent financial reporting may be caused by management's efforts to manipulate revenue to deceive users of financial statements by influencing their perceptions of entity performance and profitability. Such income manipulation can start with small actions or an inappropriate change of assumptions and change of reasoning of management. Pressures and incentives can drive up these actions until they reach the stage of fraudulent financial reporting. Such a situation could occur when, owing to pressures to meet market expectations or a desire to maximize performance gains, management adopts a position that leads to fraudulent financial reporting through significant misstatement of financial statements.

Numerous authors highlight the following financial fraud schemes:

Table no.2 *Types of financial fraud in the sense of different authors*

Nr. crt	*Rezaee (2009)*	*Albrecht, W.Steve et al.(2009)*	*Golden et al. (2009)*	*Wells (2008)*	*Singleton (2006)*
1.	*Inadequate recognition of income*	*Income fraud*	*Coordination*	*Active / Exaggerated income statements and low value statements*	*Coordination differences*
2.	*Exaggerated statements of assets other than claims*	*Cost fraud of sold goods*	*Inadequate accounting evidence for construction contracts*	*Coordination differences*	*Fictive incomes*
3.	*Statement of Expenditure / Liabilities*	*Reducing liabilities*	*Transactions with associates*	*Fictive incomes*	*Hidden liabilities*
4.	*Illegal appropriation of assets*	*Exaggerated asset fraud*	*Deduction of income and receivables*	*Passive and hidden spending*	*Inappropiate notifications*
5.	*Strong notification*	*Inappropriate notifications*	*Increase in value of receivables*	*Inappropriate notifications*	*Inappropriate asset valuation*
6.	*Various other techniques*	*Other types of fraud in financial reports*	*Inappropriate keeping of accounting records*	*Inappropriate asset valuation*	
7.			*Other misappropriation schemes*		

Source:author's concept

Inappropriate income declaration is willingness to accept income recognition alternatives and is the facility to recognize net income manipulation by using income and receivables. An inappropriate evaluation of activelolr involves the frustration of frustration of fortunes or claims. Another inappropriate valuation of the asset includes manipulation of the acquisition cost of an enterprise for the purpose of increasing future earnings, incorrect classification of fixed assets and other assets, or inappropriate inventory capitalization or start-up costs.

The easiest way to identify the minimization of fraudulent exposures is to identify transactions that involve debt and that can be understood.

As a result of an analysis of the literature, it has been observed that the most common schemes encountered in financial fraud are:

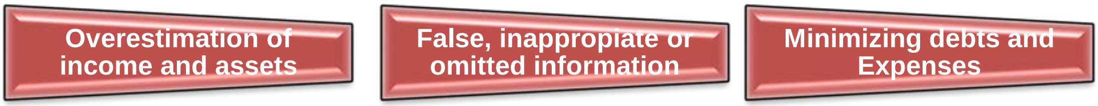

Figure no.2 *Frequent Fraud Schemes*

These schemes are designed to deprive consumers of information that shows the true position of society, so it is very important to analyze the budgets of the companies.

4. ERROR - UNNATURAL DENOTATION IN THE STATUTORY AUDIT OF FINANCIAL STATEMENTS

Each entity and business is characterized by certain features, so there are limited chances of meeting the same treatments or accounting policies appropriate to the entire flow of activities applied by two different companies.

For various reasons, either because of the complexity of the activity or the frequent changes in regulations and applicable rules, either due to personnel fluctuation, or simply omission, incomplete or other error, the accounting statements transmitted to analyzed within the Financial Audit Mission may include a series of errors that, by failing to correct them, would distort the financial statements that are being prepared.

We propose to present some types of errors identified in the practice of the economic entities and signaled by the specialized literature as well as solutions for minimizing the risk of their occurrence:

Table no.3 *Common errors encountered in the statutory audit of financial statements*

No.	Errors encountered in practice	Risk identification	Proposed solutions
1.	Erroneous transfer of the reserve from the revaluation reserve account (105) to the surplus reserve account made from revaluation reserves	Classification error generated by misrepresentation of revaluation reserve accounts and surplus reserve from revaluation reserves	Keeping a clear evidence of the evolution of the results of the revaluation of fixed assets and revaluation reserves at the level of each fixed asset
2.	Recording of reimbursement/ reimbursement revenues in a financial year different from the	Distortion of revenue and expense accounts and their corresponding accounts (asset,	Recording income and expenses related to the provision of services in the financial years to which they refer, even if these accounting records are made on the basis of proforma estimates / invoices

No.	Errors encountered in practice	Risk identification	Proposed solutions
	one in which the service was rendered	liability, result accounts)	
3.	Registering the purchase / delivery of goods in a financial year other than that in which the transfer of rights and obligations regarding the respective commodity has taken place	Distortion of stock accounts and their corresponding accounts	The company must keep a clear record of the delivery conditions related to the acquisition and/ or delivery operations and take them into account so that each transaction can be recorded in the financial year in which the transfer of the rights and obligations relating to that good takes place, INCOTERMS
4.	Erroneous diminution of supplier account balances (401) with debit balances representing advances (409)	Classification error generated by the misstatement in the balance sheet and in notes of the value of the debts and receivables, respectively advances paid to the suppliers	When recording settlement with suppliers, it is necessary to check the suppliers' balances and correct reclassification in the advances account of the value of the payments that exceed the existing debt.
5.	Presentation of good execution guarantees as commercial debt	Error classifying and presenting debts in financial statements	Companies must analyze the nature of the liabilities, and they should be recorded according to their nature in the appropriate account for fair presentation in the financial statements
6.	Omissions in the distinct presentation of transactions with affiliated parties in the financial statements	Error in the distinct presentation of transactions and balances arising from transactions with affiliated parties in the financial statements	The presentation of transactions with affiliated parties and the balances generated by these transactions requires that they be made on the basis of a list of affiliated parties, in accordance with the structure of the group.
7.	Incorrect cancellation of provisions and impairment adjustments	Distortion of income and expense accounts on provisions and impairment adjustments	The cancellation of provisions and impairment adjustments is warranted to be recorded by debiting the liability account in which the provision or impairment adjustment was reflected and not the reversal of the transaction initially recorded for the creation of the provision or impairment for impairment.
8.	Incorrect registration of received trade discounts	Error categorizing discounts and misrepresenting expense accounts and	When registering reductions received from suppliers, the nature of the reductions should be analyzed, the type of reduction determined according to the criteria set out above, as well

No.	Errors encountered in practice	Risk identification	Proposed solutions
		related revenue	as the recording of the amount of discounts in the account corresponding to their type.
9.	Revaluation of debts and debts in foreign currency at the end of the financial year	Distortion of accounts receivables, respectively debts and of income and expense accounts of foreign exchange differences	Revision of assets and liabilities and appropriate revaluation of accruals and debts identified at the exchange rate at the end of the financial year.
10.	Omissions in establishing the adjustment for impairment of receivables	Distorting the value of the adjustment for impairment of receivables	In calculating and recording the amount of the adjustment for impairment of receivables, we consider taking into account both the length of the receivables and the other factors mentioned above, which could provide indications of the chances of recovering claims.

Source :10 erori frecvente identificate in cursul auditului statutar al situatiilor financiare,Oana Bendovski, Revista Audit Financiar, nr.115, luna iulie 2014

5. Conclusions

The management and conduct of financial activity in an enterprise or in a financial institution is realized through decisions with a financial-decision content, as the mode of human action, presupposes the transition from potency to act in terms of efficiency, the basis of scientific and purposeful substantiation and motivation.

It is impossible to provide adequate and trustworthy information if the receivables in the balance sheets are presented higher than they are in reality and the assets are lower than in reality.

Currently, due to the fact that core capital is quoted on the Stock Exchange, almost all acts of corruption are carried out by committing fraud in the balance sheet. In fact, managers are trying to show that cormic companies are profitable, although they are at a loss, in order to obtain profits, so investors and creditors are misled.

In order to reduce both the risk of error and of fraud, it is necessary to implement control measures. Another measure of control would be the separation of responsibilities so that different persons and in separate positions to each other to deal with the approval of registration, registration and verification of the registration.

Future approaches include revising changes to applicable laws and regulations in the accounting field - which are not adequately addressed - would lead to material misstatement of the financial statements.

With these changes, companies must adapt the accounting treatment in accordance with the new provisions, so that financial statements to be prepared in accordance with up-to-date laws and regulations.

Since these changes in treatment need to be put into practice quickly, there is a risk that the new approach may not be fully understood or there is insufficient guidance in this respect, which may lead to errors in the accounting treatment of items falling under the incidence of changes made.

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